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CITATIONS

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433532—41

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 781

ROYAL INDEMNITY COMPANY, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The memorandum opinions of the United States District Court for the Western District of Kentucky (R. 51–52, 61–63) are unreported. The opinion of the United States Circuit Court of Appeals for the Sixth Circuit (R. 82–86) is reported in 120 F. (2d) 136.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 4, 1941 (R. 81). A petition for rehearing was filed August 4, 1941 (R. 89) and

denied October 9, 1941 (R. 119). A petition for writ of certiorari was filed December 4, 1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether a surety on a bond given to stay collection and secure payment of a tax pending disposition of a claim in abatement filed by the principal, against whom the tax was assessed, may avoid liability on the ground that the assessment was invalid and that therefore the Commissioner was without power to reject the claim.

2. If not, whether in any event the surety was discharged to the extent of an amount which the principal voluntarily contributed to its parent company and which was paid to the United States by the latter in part satisfaction of the latter's consolidated tax liability.

STATUTES INVOLVED

The pertinent portions of the Revenue Act of 1918, c. 18, 40 Stat. 1057 are set forth in the Appendix, *infra*, p. 10.

STATEMENT

This suit was brought by the United States against Louisville Woolen Mills, as principal, and Royal Indemnity Company, petitioner herein, as surety, to recover upon a common law bond given

to stay the collection and secure the payment of certain income and excess profits taxes pending determination of a claim in abatement filed by the principal. Summons was returned unexecuted as to the principal and there was no appearance by it (R. 9). Recovery against petitioner in the amount of $32,341.24 with interest was allowed by the district court (R. 65). Its judgment was affirmed by the court below (R. 86). The essential facts, as alleged in the complaint and admitted by the answer, are as follows:

In its tax returns for 1918, Louisville Woolen Mills, a Kentucky corporation, reported a tax liability of $129,364.93, which amount was duly assessed by the Commissioner of Internal Revenue (R. 2, 12). After payment of $96,843.71 of the tax so assessed, the taxpayer, on December 15, 1919, filed a claim for abatement of the unpaid balance of $32,341.24 on the ground that it should receive the benefit of a lower assessment authorized by Section 327 (d) and Section 328 of the Revenue Act of 1918 (R. 2–3, 12). The bond in suit was executed on the same date (R. 3, 12). It provided that:

> * * * in consideration of withholding collection of the said taxes * * * until such time as the Honorable Commissioner of Internal Revenue may pass upon the claim for abatement of the said assessed taxes * * * , and in order to protect the United States Government and Elwood

> Hamilton, Collector of Internal Revenue * * *, against any loss, cost or damage by reason of the said claim for abatement, the Louisville Woolen Mills, of Louisville, Kentucky, principal and the Royal Indemnity Company, of New York, surety, hereby bind themselves, jointly and severally * * * to pay to the said Elwood Hamilton, * * * the sum of $32,341.24, or as much thereof, if any, as the said Louisville Woolen Mills may be required * * * to pay on account of said assessment, together with interest thereon at the rate of one percent per month * * *; and, further, to pay the sum of $32,341.24, or as much thereof, if any, as the Honorable Commissioner of Internal Revenue shall find from his rulings to be due to the United States of America from the said Louisville Woolen Mills on account of the said assessment, with interest thereon * * *.

On August 23, 1932, while the bond was still in effect and the tax secured by it remained unpaid, the Commissioner wrote a letter to the taxpayer stating the following (R. 5–6, 16):

> Your claim is for abatement of part of the tax reported on your separate 1918 return and is a claim for special assessment under sections 327 and 328 of the Revenue Act of 1918. During the year 1918 your company was a subsidiary of American Textile Woolen Company, and computa-

> tion of the profits tax of the consolidation under sections 327 and 328 of the Revenue Act of 1918 was allowed by the Bureau. The Bureau's computation of the consolidated tax was appealed to the United States Board of Tax Appeals by your parent company on an issue relative to the allocation of the tax, and the Board's order entered January 16, 1932, in effect allocates to your company the amount of tax previously assessed on your return. Your claim for the abatement of part of such assessment will therefore be rejected.

Thereupon the Commissioner rejected the claim for abatement (R. 6, 16). The present suit was instituted after the taxpayer and petitioner had failed and refused to comply with the Collector's demands for payment of the $32,341.24 due with interest (R. 6, 17).

ARGUMENT

1. The principal contention (Pet. 10, 16–24) made by petitioner is that the decision in *American Textile Woolen Co.* v. *Commissioner,* 23 B. T. A. 670 (1931), affirmed, 68 F. (2d) 820 (C. C. A. 6), certiorari denied, 293 U. S. 558, precluded the Commissioner from rejecting the claim for abatement. It was there determined that under the consolidated return provisions of Section 240 of the Revenue Act of 1918 (Appendix, *infra,* p. 10) the American Textile Woolen Company was properly assessed to pay the taxes upon the com-

bined income for 1918 of it and its affiliated subsidiaries, of which Louisville Woolen Mills was one, since the evidence showed an agreement among them that the taxes should be so assessed. Petitioner construes this as a holding, in effect, that the prior assessment of $129,364.93 taxes against its principal, Louisville Woolen Mills, was erroneous and hence that the unpaid balance of $32,341.46 secured by the bond was not owing. It contends (Pet. 21–22) that for such reason the Commissioner had no discretion to require payment of any part of the amount last mentioned, that his action in purporting to do so was a nullity, and that, accordingly, it is not liable on the bond.

Thus petitioner seeks to avoid its obligation by attacking collaterally the validity of the Commissioner's denial of the claim for abatement. But this it may not do. The condition of the bond was that it would pay all or so much of the unpaid balance of the tax assessed as its principal "may be required to pay" or as the Commissioner "shall find from his rulings to be due," and it is settled law that such a promise creates an independent liability which cannot be avoided on the ground that the tax secured was uncollectible or in fact not owing. It is enough that the condition of the bond occurred, whether the Commissioner's ruling was right or wrong. *United States* v. *John Barth Co.*, 279 U. S. 370; *Gulf*

States Steel Co. v. *United States,* 287 U. S. 32; *Bowers* v. *American Surety Co.,* 30 F. (2d) 244 (C. C. A. 2d), certiorari denied, 279 U. S. 865; *Miami Valley Fruit Co.* v. *United States,* 45 F. (2d) 303 (C. C. A. 5th), certiorari denied, 283 U. S. 841; *Simmons Mfg. Co.* v. *Routzahn,* 62 F. (2d) 947 (C. C. A. 6th), certiorari denied, 289 U. S. 751; *Maryland Casualty Co.* v. *United States,* 76 F. (2d) 626 (C. C. A. 5th); *United States* v. *Oswego Falls Corp.,* 113 F. (2d) 322 (C. C. A. 2d).

No unjust enrichment of the Government or other unfairness results from holding petitioner to its word. The bond fulfilled its purpose of staying collection of the tax pending determination of the claim for abatement, and, if it had not been given, the tax presumably would have been collected. Cases, *supra.* No assessment covering Louisville Woolen Mills' income for 1918 was made against the American Textile Woolen Company until nearly two years after the claim for abatement was filed (23 B. T. A. 670, 677; see Pet. 5). In thereafter finally computing the tax which was due from American, the Commissioner allowed a credit of $395,610.74 representing the total of all assessments previously made against it and its subsidiaries, including the full amount of the assessment against Louisville Woolen Mills (23 B. T. A. 670, 682–3; R. 84). The rejection of the claim for abatement, therefore, did not

have the effect of twice taxing the same income, and recovery upon the bond herein results in no unjust enrichment.

2. Petitioner contends (Pet. 11, 29–33) that in any event the court below erred in not according it the benefit of $30,000 contributed by its principal in 1921 to American Textile Woolen Company and by the latter paid to the United States. Admittedly, however, the principal contributed that amount voluntarily and not on account of the assessment against it secured by the bond (R. 27). Nor was any portion paid to the Government on that account. The entire amount was paid, on the contrary, in part satisfaction of American's consolidated tax liability, not merely for the year 1918, but for 1917 and 1919 as well (23 B. T. A. 670, 677; 68 F. (2d) 820, 823).[1] Accordingly, there is no basis for petitioner's claim that its obligation on the bond was released pro tanto.[2]

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[1] For the year 1918, the *pro rata* share of Louisville Woolen Company for the consolidated tax liability of American was $167,520.57, computed on the basis of the respective net incomes of the affiliated companies (23 B. T. A. 670, 682). As noted by the court below (R. 85), this amount was more than the total tax of $129,364.93 assessed against Louisville separately plus the $30,000 contributed by it to American.

[2] The cases cited by petitioner are inapplicable since the payments by the principals there involved, which were held to release the sureties pro tanto, were on account of the debts which were secured by the bonds. *Columbia Digger Co.* v. *Rector*, 215 Fed. 618; *United States* v. *Brent*, 236 Fed. 771; *United States to Use of Thomas* v. *Morgan*, 111 Fed. 474.

CONCLUSION

The decision below is correct. There is no conflict of authority. The petition should be denied.

Respectfully submitted.

CHARLES FAHY,
Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
J. LOUIS MONARCH,
PAUL R. RUSSELL,
Special Assistants to the Attorney General.
H. G. INGRAHAM,
Attorney.

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